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January 26, 2010

TO: Each Supervisor

FROM: John F. Schunhoff, Ph.D.
Interim Director

SUBJECT: **DEPARTMENT OF HEALTH SERVICES' (DHS) FISCAL OUTLOOK, SUPPLEMENTAL INFORMATION (Agenda Item #S-2, January 26, 2010)**

This is to provide you with additional information on impacts on DHS' fiscal outlook from the State budget.

**ADDITIONAL INFORMATION CONCERNING THE GOVERNOR'S PROPOSED BUDGET**

In the Department's initial January 26, 2010 fiscal outlook report, we indicated that we anticipated a significant negative impact from the proposed $750 million reduction in State General Funds for the Medi-Cal program, but could not determine an estimate without more detailed information. Subsequently, we have learned that the Governor's proposed budget assumes continuation in FY 2010-11 of reductions to the Safety Net Care Pool (SNCP) and the South LA Fund, which will decrease our projected revenues for 2010-11 by $24 million, resulting in a corresponding increase in the projected two-year cumulative deficit to $600.7 million. This reduction is <u>in addition to</u> any reductions which would result from the $750 million reduction, because it is already assumed in the base.

**STATE USE OF COUNTIES' CERTIFIED PUBLIC EXPENDITURES FOR FY 2009-10**

Included in the adopted State budget for FY 2009-10 is $1 billion of Medicaid flexibility, which the State administration proposed to negotiate with the federal Centers for Medicare and Medicaid Services (CMS). The details of this were undefined at the time of budget passage in July. Subsequently, we informed you that the State had indicated that the components to achieve the $1 billion included use by the State of two sources of federal funds related to the Waiver. The first is $360 million which was unspent in the first two years of the Waiver and the second is $330 million, which is the amount of increased Federal Medicaid Assistance Percentage (FMAP) attributable to the SNCP.

To obtain both the $360 million and the $330 million, and other funds to achieve the $1 billion, the State needs state/local expenditures to draw down the Federal reimbursement. Last week, State staff told us that they had encountered difficulty in identifying eligible State funds which CMS would approve for this purpose. Then they stated that they were planning to use the counties' excess Certified Public Expenditures (CPE) to draw down these federal funds. [Note: Counties and their public hospitals have excess CPEs because of various limits on drawing down federal funds such as the DSH program cap, etc.] The State use of these CPEs raises a number of issues with serious implications for ongoing funding of this Department.

For FY 2009-10, a key issue is whether the state has to rely entirely on the local CPE. If so, the $1 billion needed by the State exceeds unused CPEs in the counties and if taken by the State, could limit our ability to draw down all of the DSH funding for which we are eligible this year. A related issue is that we always have some cushion of additional CPEs, so that if some costs are questioned in a future audit and found not to be eligible, there are still costs to justify the full amount of federal funds. If the State uses all of our excess CPEs, then an audit finds exceptions in future years, the federal government will look to the County to repay the funds.

The most troubling aspect of the CPE proposal is the precedent it sets for future years. This will be the first time that local public hospital CPEs in California have been used for anything but local services and programs. When the current waiver was approved in 2005, the State removed most State general funding from the inpatient programs in public hospitals and the public hospitals use their own CPEs to draw down the federal reimbursement. This goes even further, by using local expenditures to bail out the State general fund.

If the State's use of the local CPEs extends into FY 2010-11, it will jeopardize our ability to receive additional Federal funds as part of the next Waiver. As shown in the fiscal forecast, it is critical for the County to receive additional federal funding in the next Waiver. Otherwise, we will have no alternative than to recommend service reductions. If Medicaid expansion is funded under federal healthcare reform, we will at least need additional funding to bridge the gap until it begins. If Medicaid expansion does not occur, we will need five-year additional funding to treat the population which would have been covered by the expansion.

If you have any questions or need additional information, please let me know.

JFS:ws

c: Chief Executive Office
County Counsel
Executive Office, Board of Supervisors